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SUBJECT: SLOVAK BANKING SECTOR CALM IN GLOBAL STORM

SUMMARY

¶1. (SBU) The banking scene here is calm, as Slovak banks have been largely insulated from the crisis by practicing conservative banking. The government has put in place an unlimited guarantee on deposits and some restrictions on moving short-term assets to foreign parents of banks. PM Robert Fico has reassured the public that the banks are stable, and that the government, as the only responsible player, will protect its citizens and thus, regrettably, the banks. The real risks to the Slovak economy lie in the longer-term effects of the crisis on the real economy, particularly export demand and real estate; a consensus forecast of about 4-4.5 percent GDP growth is forming, down from 6.5 percent. Unless consumer demand in the Western economies begins to falter visibly, Slovaks are assuming the wave will pass. End summary.

SLOVAK BANKS "TOO PRIMITIVE" TO HARM

¶2. (U) Bankers and regulators alike have so far kept their calm in the face of the global banking crisis, and they have offered a simple explanation: banks in Slovakia have followed conservative business practices. As an official at the central bank (the National Bank of Slovakia, or NBS) put it, the banking sector here is "too primitive" to be susceptible to the crisis. Most bankers would agree: they have strong liquidity within the country and have funded loans mostly with deposits. Mortgages have followed traditionally strict qualification criteria, and there is nothing approaching a subprime market here. Slovakia being a high-growth market with high demand for deposits and an underdeveloped debt market, banks have not been tempted to add exotic derivatives from foreign markets to their balance sheets.

¶3. (U) A senior official at the central bank told us that banks doing business in Slovakia have if anything an excess of liquidity, which they park in sterilization accounts at NBS. This means that there is no interbank lending--another layer of insulation from the liquidity crisis.

PROACTIVE ON PREVENTION

¶4. (SBU) Still, with other European countries adopting aggressive measures to deal with the crisis, the Slovak government has been loath to stand still. As a measure to prevent money from crossing the Austrian border for higher guarantees, the GoS has instituted an unlimited guarantee on

deposits. At least some observers have told us this was an unnecessary step, given that there was already a guarantee for 90 percent of deposits up to 20,000 Euro. It is thought that bumping the guarantee to 100 percent would have stopped any trickle westward, which to this point has not been measurable.

¶5. (SBU) Another concern has been that the overwhelmingly foreign-owned banks here (of the top 20 banks, Slovaks own only 3) may be in danger of having their parent companies pull short-term assets across the borders to solve their own liquidity problems. Again, industry insiders tell us that there have thus far been no moves to do this. Nevertheless, the GoS has, with the approval of the industry, imposed restrictions on the movement of liquidity from Slovak subsidiaries.

¶6. (SBU) Predictably, PM Robert Fico has taken the opportunity to lambaste capital markets and portray himself as the defender of the people against rapacious capitalists. In his version of a confidence-building statement after the Brussels summit last week, Fico made the observation that the banks are liquid and stable, and that the GoS would take whatever measures are needed to keep them that way. After saying that the GoS would not look for ideologically pure solutions, he took a swipe at the markets: "The government behaves itself responsibly, morally, and ethically; the markets are waiting for whatever the government is going to do, and then they'll do more of whatever they want, because unlike governments, markets don't recognize either morality, nor responsibility, nor ethics."

THE REAL RISKS: EXPORTS AND REAL ESTATE

¶7. (SBU) The larger risk to Slovakia is seen as coming from a slowdown in the real economy both beyond and within its borders. The GOS appears to be particularly concerned about a potential drop in demand for exports, which have been responsible for a large share of economic growth since 2000. Already, Volkswagen is rumored to have seen a 10 percent drop in orders, and other export-oriented companies are now revising their forecasts downward. This could affect the revenue assumptions in the draft budget, which currently projects 6.5 percent growth for 2009 (a conservative number when it was adopted at mid-year, when real growth looked to be around 8 percent). But even the downside scenario is not gloomy; a consensus seems to be forming around an enviable 4-4.5 percent growth.

¶8. (U) An internal source for slowdown could be real estate. Slovakia, and particularly Bratislava, have seen sharp increases in real estate prices over the past several years, and an economic downturn could threaten the demand for office space, as well as the mortgages behind overpriced properties. Even so, economic experts here report that Slovakia has seen little wealth effect, so there should be relatively few ramifications from a setback in property prices, at least in comparison with other inflated real estate markets. As to other risks for consumers, there is little participation in equities or money markets (except for second pillar pension funds, which are not seen as subject to wealth effect), and so little knock-on effect from faltering global markets.

COMMENT: THE USUAL CAUTIOUS OPTIMISM

¶9. (SBU) The general thinking here is that Slovakia, along with much of the rest of the region, has dodged a bullet. There is some genuine worry about the medium-term effects of the crisis, but not much consensus. Strong fundamentals leading up to the crisis lead experts to think that the wave

will pass, and the rich countries will go back to business as usual after a couple of bad quarters. The notion that the last several years' growth was based on a credit bubble has yet to sink in, nor has the generally gloomy tone of pronouncements from the U.S. and Western European capitals. Once the crisis weakens consumer demand in the West, the Slovaks will likely grow more worried.
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